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Terrible financial year ends with hope of bright future

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By Jeff Salway
INVESTORS can take a deep breath as they reflect on 12 months in which their worst fears were never quite realised. But while there is tangible evidence of a recovery, confidence among investors remains fragile. Markets ended the year on a brighter note than many would dared to have suggested nine months ago. The FTSE, which began 2009 at 4,561, reached its lowest point in six years in March, falling to 3,512, with banking shares taking a hammering. It has s
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ince recovered, but the mood among Scottish investors remains uncertain at best.

But what do the experts think lies in store for investors this year? We asked some of Scotland's leading investment pundits for their predictions:

Alan Steel, chairman of Alan Steel Asset Management
Last year the consensus was gloomy. Now, not only is it still gloomy, but we also hear of double dips, inflation worries and a jobless recovery, among other concerns. But if you look behind the headlines you will find good reason to believe that the surprises will continue. What are they?

The US is emerging stronger than anyone believes and the dollar is not going to sink into the hole that many people expected.

Another surprise should be the continuing bull market in developing countries including India and China, not to mention the Asian tiger economies and Latin America. Economic research points to secular bull markets there, suggesting years of outperformance. Expect stock market corrections early in the year, but that should represent another good buying opportunity for optimists. The final surprise will probably be bad news for sovereign bond and deposit holders.

Tom Munro, director of Tom Munro Financial Solutions
The coming year is shaping up to be an interesting one and I favour two sectors, the first of which is global bonds. Investors saw double digit returns this year from the UK sterling bond sector, but if you haven't done so already, I would quietly head for the exit as the sparkling returns of 2009 have been and gone, with rising prices driving down yields and making the sector less attractive.

For the more adventurous I still favour emerging markets, especially China. Although Chinese stocks virtually trebled between 2005 and 2007, only to fall heavily in 2008 before rebounding sharply again this year, a sharp correction could be on the cards in the short term, but this should not deter you from sticking with what remains a fantastic long-term investing opportunity. The likes of First State offer a combination of China-only funds or diversification through their Global Emerging Market Leaders funds.

Douglas Roberts, senior international economist, global strategy, at Standard Life Investments
Much of the global economy remains in need of continued government support. In many countries it has been deemed necessary to extend fiscal support packages beyond their scheduled span, and extremely

accommodative monetary conditions are largely still in place. Despite this broad range of policy support, none of the major economies looks strong enough to do without it and there will be further challenges in 2010, amid political uncertainty. We have already had a "political" Pre-Budget Report ahead of the general election and there are likely to be similar machinations ahead of the US mid-term elections later in 2010.

Consequently, policy decisions will not be wholly driven by economic criteria. And the financial system is still not fully functional as its efforts are focused more on rebuilding their capital base than extending loans. This all suggests that economic growth will generally be less robust than would be expected in the year following recession.

Ken Taylor, managing director of Mackenzie Taylor Wealth Management
Having called the spectacular returns from good corporate bond funds and overseas equities, plus the further decline in property prices for 2009, I underestimated the strength of the upwards move in UK equity indices. The rally since March has been surprisingly strong, so guessing what the returns might be in 2010 is tricky.

The early part of the year will provide a growing realisation of the extent of our economic woes in the UK. There will be further bad news from the banks, with at least one full nationalisation likely, and the consolidation of life offices will continue, as they still represent a very inefficient market. This may take the form of closures to new business, or a rise in the number of so called "zombie" offices.

Interest rates will remain at historically low levels in the UK throughout 2010 as any recovery is likely to be patchy at best. Sadly, this means further rises in unemployment are inevitable.

House prices will remain broadly static throughout the year. And I believe that the election may well produce a surprising result in the spring.

David Thomson, investment director of VWM
On New Year's Eve 1999, the FTSE100 reached its highest ever value; nearly ten years later it is still some 25 per cent below that point. You would have been much better off investing in gilts, where your returns would have been 5.7 per cent a year. Residential property would have been an even better investment, with 7.2 per cent annualised growth over the past ten years even after the recent setback.

So clearly taking the risk in equities over the past ten years has not paid off. A terrible decade for equities is rare but not unprecedented. In the US, where the indices are more consistent (the FSTE100 was only established in 1984) there have been three other decades in the last century when the S&P 500 has failed to deliver positive returns, most recently the ten years to 1982.

Interestingly the next ten years were great for stocks – after 1982 the gains were a staggering 19.2 per cent. While this will not necessarily be repeated, there is some logic to it. After a decade of price falls, the cost of entering the market is less. Whether it is low enough relative to alternatives depends on your appetite for risk. And what about these alternatives? There is a question over whether or not it's too early to get back into property and it looks as though now is the time to be exiting from gilts as returns of the past decade are unlikely to be repeated.

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